

Generally, persons who provide subscribers access to the Internet and who do not, as part of that service, charge customers for the line or other transmission charges which are used to obtain access to the Internet, are not considered to be telecommunications retailers from these activities. See, 86 Ill. Adm. Code 495.110. (This is a GIL.)

January 8, 1999

Dear Ms. Xxxxx:

This letter is in response to your letter dated November 2, 1998. The nature of your letter and the information you have provided require that we respond with a General Information Letter which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

On behalf of our client ('Client'), we respectfully request a ruling regarding the application of Illinois' sales and use tax and telecommunications taxes to the business activities outlined below.

FACTS

General

Client is in the business of providing subscriptions to an Internet-based e-mail service. The subscriptions will be sold to individuals and businesses. Client's e-mail service is available to subscribers on a nation-wide basis by way of a toll-free 800 number. Though Client's primary service is e-mail, Client's service has the capability for subscribers to send (not receive) facsimiles. Client's initial strategy is to sell its e-mail service for a flat-rate monthly fee with a separately stated additional charge for facsimile services. At some point, Client may change its pricing strategy to be based upon subscriber usage as opposed to a flat-rate fee structure. Client makes no sales of tangible personal property.

Client licenses software to original equipment manufacturers ('OEMs') to be embedded into hand-held communication devices ('devices') which the OEMs manufacture. Client receives royalties from the OEMs for the use of its software. All OEMs are located outside the United States. The OEMs sell the devices to third party retailers which, in turn, sell such devices to potential subscribers. Client is not involved in the retail or wholesale sales of the devices.

The devices utilize audio coupling technology (Client's software) to communicate with Client's computer server. This audio technology allows subscribers the ability to use the devices with any telephone

(wireless or wireline) to access Client's server. Client's server is located in a state other than Illinois.

Nexus Considerations

As noted above, Client's server is located in a state other than Illinois. Client currently does not maintain a point-of-presence network in Illinois, though may establish a point-of-presence network in the future. A point-of-presence typically consists of leased space with modems and routing equipment.

As part of Client's sales/marketing strategy, it is anticipated that in-store sales personnel, of unrelated third-party retailers located in Illinois, selling Client's service-enabling device will refer potential subscribers to Client. In some instances, the in-store sales personnel may make sales demonstrations of the device and Client's e-mail service. In order to facilitate the selling efforts of the retailers, Client may train representatives of the retailers in the use of the service. The representatives would in turn train the in-store sales personnel. As an alternative, Client may train the OEMs in the use of Client's service. The OEMs would then be responsible for training the retailers. Client's training activities may or may not occur in Illinois.

Client's E-mail Service

A subscriber initiates communication with Client's server by using any telephone to dial Client's 800 number. The call is then connected to a switching station of an unrelated third-party telecommunications service provider. A Regional Bell Operating Company ('RBOC') maintains the connection between its switching station and Client's server.

Once connected to Client's server, the subscriber places the device next to the receiver of the phone, at which time information is transferred between the phone and the device via the audio coupling technology.

All applicable federal, state and local telecommunications taxes are currently paid by Client to unrelated third-party telecommunications service providers. Client does not add such telecommunications taxes to subscribers bills.

RULING REQUESTED

Client respectfully requests the following legal rulings:

1. Whether, under the facts described above, the retailers located in Illinois will likely be considered the 'agents' of Client for the purpose of establishing sufficient *nexus* between Client and Illinois to subject Client to a sales/use tax collection responsibility.

2. Whether a client-owned or leased point-of-presence in Illinois would establish sufficient nexus between Client and Illinois to subject Client to a sales/use tax collection responsibility.
3. Whether Client's e-mail service is subject to Illinois's sales or use tax and/or telecommunications taxes.
4. Provided Client's e-mail service is subject to Illinois's sales or use tax and/or telecommunications taxes, whether Client may rely on its subscriber's billing address to determine the appropriate taxing jurisdiction.
5. Whether Client is authorized to issue resale certificates to telecommunications service providers in purchasing telecommunications services for resale to Client's subscribers.

CONCLUSION

We appreciate your consideration of the matters described herein and look forward to your response. If you have any questions regarding this request, please contact Client's representative, PERSON

NEXUS

Taxpayers may use the following guidelines concerning the different types of retailers in order to determine whether a business should remit and collect Illinois Retailers' Occupation Tax and Use Tax.

An "Illinois Retailer" is one who either accepts purchase orders in the State of Illinois or maintains an inventory in Illinois and fills Illinois orders from that inventory. The Illinois Retailer is then liable for Retailers' Occupation Tax on gross receipts from sales and must collect the corresponding Use Tax incurred by the purchasers.

Another type of retailer is the retailer maintaining a place of business in Illinois. The definition of a "retailer maintaining a place of business in Illinois" is described in 86 Ill. Adm. Code 150.201 subsection (i) (see enclosed). This type of retailer is required to register with the State as an Illinois Use Tax collector (see 86 Ill. Adm. Code 150.801 enclosed). The retailer must collect and remit Use Tax to the State on behalf of the retailer's Illinois customers even though the retailer does not incur any Retailers' Occupation Tax liability.

The final type of retailer is the out-of-State retailer that does not have sufficient nexus with Illinois to be required to submit to Illinois tax laws. A retailer in this situation does not incur Retailers' Occupation Tax on sales into Illinois and is not required to collect Use Tax on behalf of its Illinois customers. However, the retailer's Illinois customers will still incur Use Tax on the purchase of the out-of-State goods and have a duty to self-assess their Use Tax liability and remit the amount directly to the State.

The United States Supreme Court in *Quill Corp. v. North Dakota*, 112 S.Ct. 1904 (1992), set forth the current guidelines for determining what nexus requirements must be met before a person is properly subject to a state's tax laws. The Supreme Court has set out a 2-prong test for nexus. The first prong is whether the Due Process Clause is satisfied. Due process will be satisfied if the person or entity purposely avails itself or himself of the benefits of an economic market in a forum state. *Quill* at 1910.

The second prong of the Supreme Court's nexus test requires that, if due process requirements have been satisfied, the person or entity must have physical presence in the forum state to satisfy the Commerce Clause. A physical presence is not limited to an office or other physical building. It is important to note that under Illinois law, it also includes the presence of any agent or representative of the seller. The representative need not be a sales representative and it is immaterial for tax purposes that the representative's presence is temporary.

TELECOMMUNICATIONS

The Illinois Retailers' Occupation Tax (commonly known as sales tax) is imposed upon persons engaged in this State in the business of selling tangible personal property to purchasers for use or consumption. The tax is measured by the seller's gross receipts from such sales made in the course of such business. See the enclosed copy of 86 Ill. Adm. Code 130.101. Transactions which do not involve the sale of tangible personal property at retail are not subject to the Retailers' Occupation Tax.

In Addition, Use Tax is imposed on the privilege of using, in this State, any kind of tangible personal property that is purchased anywhere at retail from a retailer. See the enclosed copy of 86 Ill. Adm. Code 150.101. Please note that the Department's current regulations provide that canned software is considered to be tangible personal property regardless of the form in which it is transferred or transmitted, including tape, disc, card, electronic means or other media. See subsection (a) of the enclosed copy of 86 Ill. Adm. Code 130.1935.

The Telecommunications Excise Tax Act imposes a tax upon the act or privilege of originating or receiving intrastate or interstate telecommunications in Illinois at the rate of 7% of the gross charges for such telecommunications purchased at retail from retailers. Please see the enclosed copy of 86 Ill. Adm. Code Part 495. This tax must be collected from persons by retailers maintaining a place of business in Illinois and is then remitted directly to the Department by such retailers. See Section 495.110.

Section 2(c) of the Act defines "telecommunications," and states that this term does not include "value added services in which computer processing applications are used to act on the form, content, code and protocol of the information for purposes other than transmission." Section (2)(a)(3) of the Act states that the term, "gross charge," which forms the basis for the tax, does not include "charges for leased time on equipment or charges for the storage of data or information for subsequent retrieval or the processing of data or information intended to change its form or content."

Generally, persons that provide subscribers access to the Internet and who do not, as part of that service, charge customers for the line or other transmission charges which are used to obtain access to the Internet, are not considered to be telecommunications retailers. See 86 Ill. Adm. Code 495.100(d). It is our general understanding that most Internet access providers do not, as part of their billing, charge customers for such line charges, but instead, pay to their telecommunications providers all transmission costs that they incur in providing the service. Generally, the customers pay to their providers all transmission costs that they incur while using the service. The single monthly fee charged by such retailers, which often represents a flat charge for a package of items including Internet access, E-mail, electronic newsletters, templates for creating web sites, and other structures that customers can use to enter data onto an Internet format, would generally not be subject to the Telecommunications Excise Tax.

However, please note that persons providing customers with the Internet access described above, but who also provide customers the use of 1-800 service, and separately assess customers with per minute charges for the use of such 1-800 numbers, are considered to be telecommunications retailers. Such retailers will incur Telecommunications Excise Tax on charges made for such 1-800 services. If, however, such Internet service providers do not separately assess customers with per minute charges, but pay their own providers for all transmission costs for the 1-800 service, they would not be considered to be telecommunications retailers.

If Internet access service providers provide both transmission and data processing services, the charges for each must be disaggregated and separately identified. See 86 Ill. Adm. Code 495.100(c), enclosed. The statute does not require disaggregation on the customers' invoice, however. Therefore, it is the Department's position that so long as the non-telecommunications charges are disaggregated from the telecommunications charges in the retailers' books and records, for audit purposes, such disaggregation need not be shown on the customers' invoice. If the non-telecommunications charges are not disaggregated from the telecommunications charges, the full amount will be subject to Telecommunications Excise Tax. If none of the charges billed are for telecommunications, then none of the charges would be subject to tax.

Section 2(n) of the Act provides that "'[s]ervice address' means the location of telecommunications equipment from which the telecommunications services are originated or at which telecommunications services are received by a taxpayer. In the event this may not be a defined location, as in the case of mobile phone, paging systems, maritime systems, air-to-ground systems and the like, service address shall mean the location of a taxpayer's primary use of the telecommunications equipment as defined by telephone number, authorization code, or location in Illinois where bills are sent."

Please note that retailers of telecommunications who are reselling telecommunications are required to register with the Department, file returns, and remit Telecommunications Excise Tax directly to the Department. Purchases by telecommunications retailers from local and long distance carriers for line time may be purchased without incurring tax by providing these suppliers with resale certificates.

Please also note that if you make computer software available to your clients that sales of tangible personal property are subject to Retailers' Occupation Tax. (See 35 ILCS 120/1 et seq.) Please note that pursuant to 86 Ill. Adm. Code 130.1935(a), "[c]lanned software is considered to be tangible personal property regardless of the form in which it is transferred or transmitted, including tape, disc, card, electronic means or other media." A license of software is not a taxable retail sale if it meets the criteria set forth at 86 Ill. Adm. Code 130.1935(a)(1). (Copy enclosed.)

I hope this information is helpful. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Terry D. Charlton
Associate Counsel

TDC:msk
Encl.